

IN THE  
**Supreme Court of the United States**

OCTOBER TERM, A. D. 1945

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**No. 966**

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HERBERT L. STERN,  
*Petitioner,*  
*vs.*

CARTER H. HARRISON, Collector of Internal  
Revenue,  
*Respondent.*

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**PETITION FOR WRIT OF CERTIORARI TO THE  
UNITED STATES CIRCUIT COURT OF APPEALS  
FOR THE SEVENTH CIRCUIT.**

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# INDEX.

	PAGE
Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit..	1
Statement of matter involved.....	1
Jurisdiction .....	3
Questions presented .....	3
Reasons for allowance of writ.....	3
Brief in support of petition.....	7
Opinions below .....	7
Statement of jurisdiction.....	7
Statement of the case.....	7
Errors to be urged.....	10
Argument .....	11
1. The question whether findings of the Dis- trict Court are subject to more extensive review than findings of the Tax Court should be settled by this Court.....	11
2. The decision of the court below to review the District Court's findings is in conflict with the decision of other Circuit Courts	19
3. In holding that the definition of partial liquidation was "automatically" appli- cable under its literal terms without ref- erence to the surrounding facts, the de- cision below is in apparent conflict with decisions of this Court relating to the construction of definitions in the tax law	20
4. In holding that a stock redemption is "auto- matically" a distribution "in partial liqui- dation of a corporation," without refer- ence to the surrounding circumstances, the decision below is in conflict with de- cisions of several other Circuit Courts of Appeals in the same matter.....	23
Appendix .....	29

## TABLE OF CASES CITED.

	PAGE
American S. S. Co. v. Wickwire Spencer Steel Co., 8 F. Supp. 562 (D.C. N.Y.).....	13
Blair v. Oesterlein Machine Co., 17 F. (2d) 663 (App. D. C.) .....	13
Blair v. Oesterlein Machine Co., 275 U. S. 220.....	13, 14
Blumenthal Print Works v. United States, 141 F. (2d) 211 (CCA 5th) .....	4, 19
Bogardus v. Commissioner, 302 U. S. 34.....	15
Burnet v. Lexington Ice & Coal Co., 62 F. (2d) 906 (CCA 4th) .....	20
Colorado National Bank of Denver v. Commissioner, 305 U. S. 23.....	14
Commissioner v. Heining, 320 U. S. 467.....	22
Commissioner v. Kolb, 100 F. (2d) 920 (CCA 9th)....	5, 26
Commissioner v. Liberty Bank & Trust Co., 59 F. (2d) 320 (CCA 6th) .....	19
Commissioner v. Whitaker, 101 F. (2d) 640 (CCA 1st) ..	5, 26
Deputy v. duPont, 308 U. S. 488.....	15
District of Columbia v. Pace, 320 U. S. 698.....	19
Dobson v. Commissioner, 320 U. S. 489.....	3, 4, 11, 19
Exmoor Country Club v. United States, 119 F. (2d) 961, (CCA 7th) .....	15
Garden City Feeder Co., 27 B.T.A. 1132.....	13
Goldsmith v. U. S. Board of Tax Appeals, 270 U. S. 117	13
Greenbaum v. United States, 17 F. Supp. 83 (Ct. Cl.)..	13
Gregory v. Helvering, 293 U. S. 465.....	4, 21
Guggenheim v. Rasquin, 312 U. S. 254.....	14

	PAGE
Gutbro Holding Company v. Commissioner, 138 F. (2d) (CCA 2d).....	5, 26
Guy v. Donald, 203 U. S. 399.....	4, 21
Harter Bank & Trust Co. v. Gentsch, 60 F. Supp. 400 (D.C. Ohio) .....	26
Helvering v. Leary, 93 F. (2d) 826 (CCA 4th).....	5, 26
Helvering v. Morgan's, Inc., 293 U. S. 121. ....	4, 21
Helvering v. Schoellkopf, 100 F. (2d) 415 (CCA 2d) ..	5, 26
Helvering v. Tex-Penn Oil Company, 300 U. S. 481....	15
John Kelley Company v. Commissioner, .... U. S. ....., 90 L. ed. 257.....	3, 11
Lothair S. Kohnstamm v. Pedrick, 152 F. (2d) ....., 46-1 USTC par. 9122 (CCA 2d).....	20
Marsh v. Commissioner, 110 F. (2d) 423 (CCA 7th)..	15
McCaughn v. Real Estate Land Title & Trust Com- pany, 247 U. S. 606.....	14
Nachod & United States Signal Co. v. Helvering, 74 F. (2d) 164 (CCA 6th).....	13
Pinellas Ice & Cold Storage Company v. Commissioner, 287 U. S. 462.....	4, 21
Powers v. Commissioner, 312 U. S. 259.....	14
Trust Company of Georgia v. United States, 60 F. Supp. 470 (Ct. Cl.).....	25
Mabel I. Wilcox, 43 B.T.A. 931; aff'd 137 F. (2d) 136 (CCA 9th) .....	24

#### STATUTES CITED.

Judicial Code, Sec. 240(a).....	3, 7
Revenue Act of 1936:	
Sec. 115(c) .....	2, 3, 8, 10, 11, 20, 22, 23, 29
Sec. 115(i) .....	11, 20, 22, 29, 30
Sec. 117(a) .....	2, 8, 10, 30

## COMMITTEE REPORTS.

	PAGE
H. Rep. #1, 69th Cong., 1st Sess., p. 17.....	12
S. Rep. #52, 69th Cong., 1st Sess., p. 37.....	12
H. Rep. #2, 70th Cong., 1st Sess., p. 30.....	12

## TEXTS.

Eisenstein: Some Iconoclastic Reflections on Tax Administration, 58 Harv. L. Rev. 477, 541-42.....	16
Griswold: The Need for a Court of Tax Appeals, 57 Harv. L. Rev. 1153, 1154, 1170.....	15
Randolph Paul, Dobson v. Commissioner: The Strange Ways of Law and Fact, 57 Harv. L. Rev. 753, 808..	18
Stevens, Legal Evidence before the Board of Tax Appeals, 6 National Tax Magazine, 459, 461.....	16

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Herbert L. Stern, by A. J. Pflaum, Harry N. Wyatt, Richard H. Levin and Hedwig F. Brann, his counsel, prays that a writ of certiorari be issued to review the judgment of the United States Circuit Court of Appeals for the Seventh Circuit in this case.

**STATEMENT OF MATTER INVOLVED.**

During 1935 and 1936 Balaban & Katz Corporation (hereinafter for convenience sometimes referred to as "B & K"), a corporation engaged in the operation of motion picture theatres in Chicago, adopted a plan for refinancing or recapitalization, designed to substitute low interest

bank loans for high yield securities (notes and preferred stock), thereby diminishing its annual charges before common dividends. During 1936, as one step in the carrying out of this plan, B & K acquired by redemption approximately 50% of its outstanding preferred stock. The petitioner, who was a preferred stockholder of B & K at that time, realized a gain of \$22,650.16 upon this disposition of his stock and treated this gain in his 1936 income tax return as a capital gain subject to the percentage limitations of Section 117(a) of the Revenue Act of 1936. (This statutory provision and the other pertinent statutory provisions here involved are quoted in full in the Appendix hereto.)

This treatment was contested by the Commissioner of Internal Revenue on the theory that the payment by B & K for preferred stock in 1936 was governed by Section 115(c) of the Revenue Act of 1936 as "amounts distributed in partial liquidation of a corporation" and hence the gain on such payment was 100% taxable. The petitioner paid the deficiency claimed and proceeded in the regular form to seek a refund of the amount so paid.

The District Court held that the sale of the preferred stock was one step in and could not be dissociated from the plan of refinancing or recapitalization, that there was no distribution in partial liquidation of B & K within the meaning of Section 115(c) and that the gain was subject to the percentage limitations of Section 117(a).

On appeal by the respondent, the Circuit Court of Appeals for the Seventh Circuit held that the findings of the District Court were subject to review, that the transaction was a distribution in partial liquidation of the corporation within the meaning of Section 115(c) and that the gain was 100% taxable.



## JURISDICTION.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925, c. 229, § 1, 43 Stat. 938; 28 U.S.C.A. § 347(a). The judgment herein sought to be reviewed is a decision of the United States Circuit Court of Appeals for the Seventh Circuit entered December 18, 1945 (R. 132).

## QUESTIONS PRESENTED.

1. Was the finding of the District Court, that the sale of preferred stock here involved was one step in and could not be dissociated from the plan of refinancing and recapitalization of B & K and hence that payment for said stock was not a distribution in partial liquidation, subject to review by the Circuit Court of Appeals?

2. Were the amounts received by the petitioner on the sale of his B & K preferred stock in 1936 "amounts distributed in partial liquidation of a corporation" within Section 115(e) of the Revenue Act of 1936?

## REASONS FOR ALLOWANCE OF WRIT.

1. In reviewing and reversing the findings of the District Court herein, the Circuit Court of Appeals has assumed authority which it would not have had, under the applicable decisions of this Court, if the decision of first instance herein had been entered by the Tax Court of the United States.

*Dobson v. Commissioner*, 320 U. S. 489;

*John Kelley Company v. Commissioner*, .... U. S. ...., 90 L. ed. 257.

The question whether the rule of reviewability shall be different for decisions of the Tax Court and decisions of the District Courts involving the same issues is an important question of Federal law which has not been but should be settled by this Court.

2. The decision of the Circuit Court of Appeals that the findings of the District Court herein are reviewable is in conflict with the decision of the Circuit Court of Appeals for the Fifth Circuit to the effect that the rule of *Dobson v. Commissioner*, 320 U. S. 489, is applicable on review of decisions of the District Court.

*Blumenthal Print Works v. United States*, 141 F. (2d) 211 (CCA 5th).

3. The decision of the Circuit Court of Appeals that the redemption of stock in the present case was "automatically" a "distribution in partial liquidation of a corporation" as provided in Section 115(c), without reference to the attendant circumstances and without reference to the form, history and intention of the applicable statutory provisions, is in conflict with applicable decisions of this Court to the effect that definitions in the revenue laws must not be read mechanically so as to force the application of the law to transactions never intended to be covered.

*Gregory v. Helvering*, 293 U. S. 465;

*Pinellas Ice & Cold Storage Company v. Commissioner*, 287 U. S. 462;

*Guy v. Donald*, 203 U. S. 399, 406;

*Helvering v. Morgan's, Inc.*, 293 U. S. 121, 126.

4. Said decision of the Circuit Court of Appeals is in conflict with decisions of other Circuit Courts of Appeals in the same matter, to the effect that a redemption or cancellation of stock may not be dissociated from all of the attendant facts and circumstances so as to characterize the

transaction as a distribution in liquidation of a corporation where the transactions taken as a whole are not in substance liquidating.

*Commissioner v. Whitaker*, 101 F. (2d) 640 (CCA 1st);

*Commissioner v. Kolb*, 100 F. (2d) 920 (CCA 9th);

*Helvering v. Schoellkopf*, 100 F. (2d) 415 (CCA 2d);

*Helvering v. Leary*, 93 F. (2d) 826 (CCA 4th);

*Gutbro Holding Company v. Commissioner*, 138 F. (2d) 16 (CCA 2d).

These reasons are further and more fully developed in the brief in support hereof, annexed hereto.

All of which is respectfully submitted.

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